

NOT TO BE PUBLISHED IN THE OFFICIAL REPORTS

California Rules of Court, rule 8.1115(a), prohibits courts and parties from citing or relying on opinions not certified for publication or ordered published, except as specified by rule 8.1115(b). This opinion has not been certified for publication or ordered published for purposes of rule 8.1115.

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION FIVE

BURNS PACIFIC CONSTRUCTION,
INC.,

Plaintiff and Appellant,

v.

MODERN ALLOYS, INC.,

Defendant and Respondent.

B205630

(Los Angeles County Super. Ct.
Nos. KC043674/KS011799)

APPEAL from a judgment of the Superior Court of Los Angeles County, Steven D. Blades, Judge. Affirmed.

Lascher & Lascher, Wendy C. Lascher and Eric R. Reed for Plaintiff and Appellant.

Law Offices of Jeffrey D. Pearlman and Jeffrey D. Pearlman for Defendant and Respondent.

Plaintiff and appellant subcontractor Burns Pacific Construction, Inc. appeals from a judgment confirming an arbitration award. Defendant and respondent contractor Modern Alloys, Inc. withheld payment from Burns and pursued arbitration of a billing dispute. The arbitrator found Modern was not entitled to payment from Burns. On appeal, Burns contends statutory prompt payment penalties should have been assessed against Modern under Public Contract Code section 10262.5,¹ because Modern's reasons for withholding payment did not constitute a good faith dispute over the amount due on a progress payment.² We hold there is substantial evidence to support the arbitrator's finding that Modern's claims were a good faith dispute over the amount due on a progress payment, and therefore we affirm.

FACTS AND PROCEDURAL BACKGROUND

In 2002, the State of California Department of Transportation (Caltrans) hired Modern to repair roads damaged by fire. Under the contract, Modern could bill work performed by subcontractors based on the subcontractor's itemized costs for labor, equipment, materials, and markups, plus a 5 percent markup on the total to Modern. Modern could bill "special forces/services" work performed by a specialist either (1) in the same manner as a subcontractor, or (2) in a non-itemized lump sum, plus a 15 percent markup on the total to Modern.

Burns submitted a written price quotation to Modern on September 18, 2002, that specified rates for certain types of operated equipment. The next day, Modern sent Burns a written purchase order. The purchase order did not specify unit prices for operated

¹ All further statutory references are to the Public Contract Code, unless otherwise noted.

² Burns's request for judicial notice filed April 24, 2008, and motion to augment the record on appeal filed August 8, 2008, are granted. Modern's request for judicial notice filed July 23, 2008, is granted.

equipment and noted the total compensation was to be determined. Modern considered Burns to be a specialist hired at the direction of Caltrans.

Modern had crews working at the site for approximately three months. During this time, Burns charged Modern non-itemized lump sums for operated equipment at the rates set forth in the September 18, 2002 quotation. Modern submitted invoices to Caltrans that included a 15 percent markup on the work performed by Burns.

After Modern completed the majority of its work at the site in December 2002, Burns began preparing the invoices in Modern's name and forwarding them to Modern to submit to Caltrans. Burns charged its operated equipment as "equipment" and "labor" at Caltrans's published rates, which were higher than the amount in Burns's quotation. Burns charged a 15 percent markup for its own subcontractors and vendors, but only a 5 percent markup to Modern. Caltrans continued to request work from Burns for another year.

In January 2004, Modern issued a progress payment that Burns never received. Burns filed a complaint against Modern seeking payment and statutory prompt payment penalties. In conducting an investigation in order to stop payment on the lost check, Modern became aware that Burns had included only a 5 percent markup for Modern instead of 15 percent. The difference between the two rates amounted to \$171,846.74. On February 26, 2004, Modern sent a letter to Burns explaining the payment dispute. Modern stated that it was withholding \$257,770.11, which was 150 percent of the disputed amount, as permitted under section 10262.5.

On April 1, 2004, Modern filed a government claim against Caltrans seeking payment of the difference that had not been billed. The claim was denied, because Caltrans considered Burns to be a subcontractor hired by Modern, rather than a specialist hired at Caltrans's direction.

Modern successfully petitioned the superior court to have Burns's action dismissed. On June 25, 2004, Modern initiated arbitration proceedings against Caltrans and Burns. The arbitration complaint alleged causes of action against Burns for breach of

contract based on a failure to invoice its work as required under Modern's purchase order and an oral subcontract. The complaint also alleged causes of action for indemnity and declaratory relief on the theory that Modern was entitled to compensation from Burns for Caltrans's failure to make payments to Modern as a result of Burns's actions. Burns filed a cross-complaint for breach of contract. Modern entered into a settlement agreement with Caltrans.

In preparing for arbitration against Burns, Modern became aware that Burns had charged the published rates for operated equipment instead of the quotation rates. Therefore, Modern sought an award of \$273,407.80, which included overbilling of \$121,302.05 on operated equipment and \$152,105.75 for the 10 percent difference in the markup rate, or if the higher rates were properly used, then Modern sought an award of \$171,864.74 for the difference in the markup rates. Burns sought the balance remaining under the purchase order of \$257,770.11, plus statutory penalties.

Evidentiary hearings were held on June 19, 20, and 21, 2006. The parties submitted closing briefs. Burns argued that it was Modern's responsibility to submit bills to Caltrans and request a 15 percent markup.

The arbitrator issued a final award on April 9, 2007, concluding that neither party had executed or verbally accepted the proposal of the other, but an implied-in-fact contract based on Modern's purchase order was created when Burns undertook performance and submitted billings that referenced the purchase order. The arbitrator found that Burns had not breached the contract by pricing labor and equipment separately at the published rates, because Modern had not accepted the equipment rates in Burns's quotation and the parties had left appropriate prices to be mutually determined as the work proceeded. Although Burns submitted bills that charged the quoted rates for three months, those prices were binding only for the work that Burns had performed and Modern had accepted at those prices that were mutually acceptable to the parties at that time. Burns was not bound to continue charging the quoted prices.

The arbitrator found Burns did not have an obligation to bill its work in a manner that would permit Modern to charge the work as special services and add a markup of 15 percent. The purchase order did not state that Burns had to charge its work as special services, Burns billed its work in a manner that was permitted for special forces by the contract with Caltrans, and Modern did not establish that Burns's work qualified as special forces work.

Under the implied contract, Burns was obligated to submit price revisions in a reasonable and timely fashion. Substantial evidence showed that Burns submitted revised prices under the billings submitted to Modern in a manner that provided a reasonable opportunity for Modern to object to the prices. The arbitrator found the pricing change constituted a new offer that was permitted under the Caltrans contract, and by failing to object and continuing to pay for Burns's performance, Modern impliedly accepted the revised prices. Moreover, Modern was not damaged, because the payments were made by Caltrans and were not a loss suffered by Modern.

The arbitrator considered whether Burns was entitled to recover penalties for the withholding of payment. The arbitrator found, "The issue is what was in Modern's mind. Second, the legal issues of duty, breach and damages presented by this case are neither as simple nor obvious as Burns characterizes them. The absence of a written contract, the parties' conduct of leaving essential terms to future agreement, the lack of any definitive agreement on essential terms, the importance of implied terms to the resolution of their dispute over billing preparation, classification of work and mark up, and the complex and sometimes ambiguous classification of work categories in the State's specifications and in the billing forms dictated by the State, are all factors that have made, and one can assume inferentially would have made from Modern's perspective, a challenging case to judge who was right and who was wrong as to the dispute that formed the basis for Modern's withholding. Absent any affirmative evidence that Modern actually believed its withholding was not legally tenable, these facts alone are sufficient, substantial evidence from which the Arbitrator infers that Modern's subjective state of mind was

within the purview of what *Alpha Mechanical[, Heating and Air Conditioning, Inc. v. Travelers Casualty & Surety Co. of America* (2005) 133 Cal.App.4th 1319] defines as consistent with good faith. Based on the foregoing, it is concluded that Burns is not entitled to statutory penalties for the withholding of funds by Modern.”

Burns filed a petition to correct or vacate the arbitrator’s award. A hearing was held on August 28, 2007. No reporter’s transcript of the hearing has been provided. Burns argued the arbitrator incorrectly applied the law as to penalty payments, or alternatively, insufficient evidence supported the arbitrator’s denial of penalty payments. Burns argued that “progress payment” meant the amount due to Burns under the contract and did not include any markup owed Modern by Caltrans. The trial court allowed the parties to submit supplemental briefing on the legal definition of “progress payment” as used in section 10262.5. On September 11, 2007, the trial court issued a minute order finding the arbitrator had carefully determined whether there was a good faith dispute, there was sufficient evidence to justify the arbitrator’s award, and the arbitrator did not commit an error of law. On January 2, 2008, the trial court entered a judgment confirming the arbitration award. Burns filed a timely notice of appeal from the judgment.

DISCUSSION

Standard of Review

Section 10240.12 provides that a party may petition the court to confirm, correct, or vacate an arbitration decision rendered in accordance with the provisions of section 10240.8, and the court shall vacate the award if it determines either that the award is not supported by substantial evidence or not decided in accordance with state law.

“We review the trial court’s rulings on [a] petition to vacate the award under the substantial evidence test, except for legal determinations, which we review independently.” (*County of Solano v. Lionsgate Corp.* (2005) 126 Cal.App.4th 741,

752.) “[T]he judgment is presumed to be correct and we must indulge all presumptions in favor of its correctness. [Citations.] In keeping with that standard, we will infer findings in support of the judgment if such findings are supported by substantial evidence. [Citation.]” (*Alpha Mechanical, Heating & Air Conditioning, Inc. v. Travelers Casualty & Surety Co. of America, supra*, 133 Cal.App.4th at p. 1338.)

Good Faith Dispute Over the Amount Due on a Progress Payment

Burns contends Modern’s reasons for withholding payment did not constitute a good faith dispute over the amount due on a progress payment under section 10262.5. We disagree.

Section 10262.5 requires a prime contractor or subcontractor to pay its subcontractors the respective amounts allowed the contractor on account of the work performed by the subcontractors within 10 days of receipt of each progress payment. “In the event that there is a good faith dispute over all or any portion of the amount due on a progress payment from the prime contractor or subcontractor to a subcontractor, then the prime contractor or subcontractor may withhold no more than 150 percent of the disputed amount.” (§ 10262.5, subd. (a).)

“Any contractor who violates this section shall pay to the subcontractor a penalty of 2 percent of the amount due per month for every month that payment is not made. In any action for the collection of funds wrongfully withheld, the prevailing party shall be entitled to his or her attorney’s fees and costs.” (§ 10262.5, subd. (a).)

“‘Good faith, or its absence, involves a factual inquiry into the plaintiff’s subjective state of mind. . . . A subjective state of mind will rarely be susceptible of direct proof; usually the trial court will be required to infer it from circumstantial evidence.’ [Citation.] In *People v. Nunn*, the California Supreme Court stated that ‘[t]he phrase “good faith” in common usage has a well-defined and generally understood meaning, being ordinarily used to describe that state of mind denoting honesty of

purpose, freedom from intention to defraud, and, generally speaking, means being faithful to one's duty or obligation.' (*People v. Nunn* [(1956) 46 Cal.2d 460, 468].)" (*Alpha Mechanical, Heating & Air Conditioning, Inc. v. Travelers Casualty & Surety Co. of America, supra*, 133 Cal.App.4th at p. 1339.)

The arbitrator found that Modern believed in good faith that Burns had not prepared invoices correctly, in breach of the parties' contract, and was liable for the shortfall. Burns itemized labor, equipment, and materials separately, and charged markups in a completely different way than it had charged Modern for the first three months of the project. Modern believed that Burns was required to set forth amounts in invoices in a certain way based on the purchase contract and the parties' prior practice. Modern's claim that Burns was liable for the amount that was not received as a result of improper billing and the amount could be deducted from payment owed to Burns was a good faith dispute over the amount due on a progress payment. (Cf. *Alpha Mechanical, Heating & Air Conditioning, Inc. v. Travelers Cas. & Sur. Co. of America, supra*, 133 Cal.App.4th at pp. 1325-1326 [contractor withheld payment to subcontractor, claiming subcontractor caused damage to other work on the project and contractor had the right to deduct for repairs under the subcontract].)

DISPOSITION

The judgment is affirmed. Respondent Modern Alloys, Inc. is awarded its costs on appeal.

KRIEGLER, J.

We concur:

ARMSTRONG, Acting P. J.

MOSK, J.